Economic Research

Irish 2016 GDP forecast cut to 2% 18 July 2016

The CSO initially estimated Irish real growth in 2015 at 7.8% and the level of GDP at €214.6bn. Substantial data revisions are not uncommon but the scale of the latest is staggering; nominal GDP last year is now put at €255.8bn, over €41bn higher than first thought, with real growth an astonishing 26.3%. Some analysts prefer to use GNP as a better measure for Ireland given the significance of multinationals in the Irish accounts (it adjusts GDP for profit and interest flows in an out of the economy) but growth on that metric was also stratospheric, at 18.7%. GNP growth in 2014 was also stellar, at a revised 9.2%, outstripping the 8.5% recorded for GDP.

The revision for 2015 primarily reflected a massive inflow of foreign direct investment in the final quarter, amounting to €130bn, which brought the annual inflow to €170bn, compared to the €20bn or so that Ireland would normally attract. Consequently, Ireland's capital stock soared, and investment spending as captured in the national accounts rose by 32.7%, driven by intangibles, the term used to cover spending on R&D. This component actually rose by 100% and the implication is that some multinationals transferred patents and copyrights to their Irish operations.

The biggest revision was to exports, however, which were deemed to have risen by over 34% in volume terms, with imports up by 22%. The latter would be boosted by spending on patents if purchased from abroad but the biggest factor at work may be aircraft leasing,; the net income from such activities was previously captured but now inflows and outflows are recorded, so boosting the gross trade figures. Moreover, under new BoP standards, it is the change of ownership which is relevant for international trade, so these aircraft do not have to enter or leave Ireland to be counted. That poses a difficulty for analyst as it is impossible to get a handle on these and other multinational export flows, and they are clearly enormous; merchandise exports as recorded in Ireland's monthly trade data amounted to €112bn, as against €195bn in the national accounts, with total exports (i.e. including services) at over €317bn. Data on services is not published on a monthly basis .

Consumer spending growth was also revised higher, to 4.5%, although this is more understandable, given the 2.6% increase in employment , contributing to an 8.5% rise in real disposable income . Consequently there was a strong rebound in the gross personal savings ratio. Government spending also rose, by a modest 1.2%, with stock building also adding to growth (0.6%)

On the revised data GDP rose by a seasonally adjusted 21% in the first quarter of 2015 so base effects alone would result in a massive slowdown in the annual growth rate. In the event the CSO announced that real GDP had actually fallen in the first quarter of 2016, by 2.1%. On the positive side consumption rose by over 2%, the best performance in a decade, boosted by car sales, and government consumption also picked up, by 1.6%. Capital spending fell sharply, however, by 16%, with declines in spending on machinery and equipment and intangibles, while exports were deemed to have fallen by 5%. Imports slumped by 10%. The annual change in GDP was still positive, at 2.3%, but a far cry from the 28% recorded in the final quarter of 2015.

Retail sales have slowed a little on an annual basis in q2 and the Brexit uncertainty may well prove a negative and so we expect consumer spending to slow over the rest of the year, although the strong start will still leave the annual rise at 4.25%. Similarly, government spending is forecast to rise by 3.0% given the 3.5% pace recorded in the first quarter. In terms of capital formation, building and construction slowed in q1, growing by an annual 2.6%, but this included a fall in housebuilding which we view as a statistical quirk . Consequently we expect the latter to pick up and support a 5% rise in construction this year. We expect stronger growth in machinery and equipment, a 10% increase, given a very weak figure last year when air-craft are excluded. The figure for intangibles is anyone's guess , however, and we have pencilled in a 20% fall, as seen in q1, although base effects means the decline over the full year could be sharper still an represents a downside risk, although if that materialised imports would also be lower.

Forecasting external trade with so many unknown flows is also problematical to say the least. We do know that exports and imports were still showing positive annual growth in q1 (1.3% and 2.6% respectively) but the published merchandise data to May shows both showing annual declines in the last few months, notably in imports. We now forecast zero growth in real exports and a fall in imports, with the risks to that on the downside given the Brexit vote. The net result is that real GDP growth for 2016 is now cut to 2.0%, with a 2.5% figure for GNP. There is likely to be a wide dispersion of forecasts around the mean given the scale of the base effects and more attention focused on those components deemed to better reflect underlying activity in the economy, which effectively means personal consumption and government spending on goods and services.

Real GDP (% change)	**2014**	**2015**	**2016(e)**	**2017 (f)**
Personal Consumption	1.7	4.5	4.3	3.5
Government Consumption	5.4	1.3	3.0	2.0
Fixed Capital Formation	18.2	32.7	-3.0	8.0
Stocks (% GDP)	1.6	0.6	0.3	0.2
Exports	14.4	34.4	0.0	3.0
Imports	15.3	21.7	-1.0	4.0
GDP	8.5	26.3	2.0	3.0
GNP	9.2	18.7	2.5	3.2

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